

AUDITOR'S REPORT OF THE AUDITOR-GENERAL TO THE WESTERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON THEEWATERSKLOOF MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Theewaterskloof Municipality, which comprise the financial position as at 30 June 2010, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information, as set out on pages 3 to 55.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and in the manner required by the Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and Division of Revenue Act of South Africa (Act No. 12 of 2009) (DoRA). This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and *General Notice 1570 of 2009* issued in *Government Gazette No. 32758 of 27 November 2009*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

7. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Theewaterskloof Municipality as at 30 June 2010 and its financial performance and its cash flows for the year then ended in accordance with SA Standards of GRAP and in the manner required by the MFMA and DoRA.

Emphasis of matters

8. I draw attention to the matters below. My opinion is not modified in respect of these matters:

Material under spending of the budget

9. As disclosed in appendix E(2) to the financial statements the municipality has materially under spent its capital budget to the value of R17 568 813. This under spending mainly affected the following service delivery areas:
 - Roads, water and electricity distribution – The environmental impact assessments and ownership of land caused delays in the commencement of the project.

Additional matter

I draw attention to the matter below. My opinion is not modified in respect of this matter

10. The supplementary information set out on pages 56 to 64 does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

11. As required by the PAA and in terms of *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*, I include below my findings on the report on predetermined objectives, compliance with the following key laws and regulations: MFMA, DoRA, Local Government: Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) and financial management (internal control).

Predetermined objectives

12. Material findings on the report on predetermined objectives, as set out on pages 1 to 66, are reported below:

Non-compliance with regulatory reporting requirements

Lack of adoption or implementation of a performance management system

13. The Theewaterskloof municipality did not adopt a framework that describes and represents how the municipality's cycle and processes of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, including determining the roles of the different role players, as required in terms of sections 36, 38 and 41(2) of the MSA, and regulations 7 and 8 of the Municipal Planning and Performance Management Regulations, 2001.

No mid-year performance assessments

14. The accounting officer of the Theewaterskloof municipality did not assess the performance of the municipality during the first half of the financial year, taking into account the municipality's service delivery performance and the service delivery targets and performance indicators set in the service delivery and budget implementation plan, as required by section 72 of the MFMA.

Usefulness of reported performance information

The following criteria were used to assess the usefulness of the planned and reported performance:

- **Consistency:** Has the municipality reported on its performance with regard to its objectives, indicators and targets in its approved integrated development plan, i.e. are the objectives, indicators and targets consistent between planning and reporting documents?
- **Relevance:** Is there a clear and logical link between the objectives, outcomes, outputs, indicators and performance targets?
- **Measurability:** Are objectives made measurable by means of indicators and targets? Are indicators well defined and verifiable, and are targets specific, measurable, and time bound?

The following audit findings relate to the above criteria:

Planned and reported performance targets not specific / measurable / time bound

15. For the selected programmes, 29 per cent of the planned and reported targets were not:

- Specific in clearly identifying the nature and the required level of performance;
- Measurable in identifying the required performed; and
- Time-bound in specifying the time period or deadline for delivery

Planned and reported indicators not well defined

16. For the selected programmes, 21 per cent of the planned and reported indicators were not clear, with an unambiguous definition to allow for data to be collected consistently.

Reliability of reported performance information

The following criteria were used to assess the usefulness of the planned and reported performance:

- **Validity:** Has the actual reported performance occurred and does it pertain to the entity i.e. can the reported performance information be traced back to the source data or documentation?
- **Accuracy:** Amounts, numbers and other data relating to reported actual performance has been recorded and reported appropriately.
- **Completeness:** All actual results and events that should have been recorded have been included in the reported performance information.

The following audit findings relate to the above criteria:

Reported indicators not reliable as no supporting source information was provided

17. For the selected programmes the validity, accuracy and completeness of 23 per cent of the reported indicators could not be established as relevant source documentation could not be provided for audit purposes.

Planned and reported indicators not verifiable

18. For the selected programmes, 30 per cent of the planned and reported indicators were not verifiable, as it was not possible to validate the processes and systems that produce the indicator.

Compliance with laws and regulations

MFMA

Expenditure was incurred otherwise than in accordance with section 15 of the MFMA resulting in unauthorised expenditure

19. Expenditure was not incurred in accordance with the approved budget of the municipality and exceeded the limits of the amounts appropriated for the different votes in the approved budget of the municipality. As disclosed in note 40.1 to the financial statements, unauthorised expenditure to the value of R8 780 520 was incurred due to the actual expenditure exceeding the approved budget.

INTERNAL CONTROL

20. I considered internal control relevant to my audit of the financial statements and the report on predetermined objectives as well as compliance with the relevant laws and regulations, but not for the purpose of expressing an opinion on the effectiveness of internal control.
21. The matters reported below are limited to the significant deficiencies regarding the basis for the opinion paragraph, the findings on the report on predetermined objectives and the findings on compliance with laws and regulations.

Leadership

- 22. The internal policies and procedures of the municipality did not adequately address the processes pertaining to the planning, monitoring, managing and reporting of performance information at the overall performance management level and objective level.
- 23. Those responsible for overseeing compliance with the MFMA did not in all instances exercise sufficient oversight to prevent irregular and unauthorised expenditure

Performance management

- 24. Pertinent information is not identified and captured in a form and time frame to support performance reporting. Adequate processes have not been implemented to ensure that sufficient appropriate evidence is maintained to support actual performance included in the report on predetermined objectives and to ensure variances are explained and targets are specific and measurable.

Auditor-General
Cape Town

30 November 2010



A U D I T O R - G E N E R A L
S O U T H A F R I C A

Auditing to build public confidence

THEEWATERSKLOOF MUNICIPALITY

TABLING OF THE ANNUAL REPORT BY THE CHAIRPERSON OF THE AUDIT AND PERFORMANCE AUDIT COMMITTEES FOR THE FINANCIAL YEAR ENDING 30TH JUNE 2010

INTRODUCTION

Madam Speaker
Mr. Mayor – The Honourable Mr. Punt
Members of Council
The Municipal Manager and Directors
Ladies and Gentlemen

It is a great honour to deliver my ANNUAL report to council for the financial year ending 30th June 2010

Congratulations to the Theewaterskloof Municipality fraternity on having received an unqualified report from the Auditor General in respect of the 2008/2009 financial year. A clean report however still evades TWKM and this is the ultimate goal to which we should all commit ourselves.

1. THE AUDIT COMMITTEE AND THE PERFORMANCE AUDIT COMMITTEE

The Audit and Performance Audit Committees of T.W.K.M are statutory committees whose duties and responsibilities are delegated to it by Council. These duties and responsibilities are clearly articulated in our audit charters which were approved by council in compliance with the MFMA.

The Audit Committee consists of five independent members who are all appropriately qualified, who are financially literate and who are acquainted with the risk management discipline.

The Performance Audit Committee consists of three suitably qualified members who have a good understanding of Performance Management as applied within Local Government.

These two committees assist council in discharging their duties with regard to:

- The safeguarding of assets
- Assurances that adequate financial systems and control processes are in place
- Assurances that financial statements are presented on a regular basis and that these statements are GRAP compliant, mindful of the fact that TWKM has adopted the transitional provision of GRAP standards with regard to GRAP 12, 16, 17, 19, 100 and 102. These include aspects relating to inventories, property, provisions for contingent liabilities etc.
- Assurances that a functional system of performance management is in place and is fully operational.

Both committees have each held a minimum 4 meetings during the financial year under review. These meetings were well attended by committee members, the municipal manager, executive directors and members of the audit team.

The chairperson of the audit committee meets regularly with the deputy director (internal audit) where matters of mutual interest are discussed. These matters include: nature of the investigations; progress w.r.t investigations, the timing thereof; agendas of meetings and review of the annual risk based audit plan.

A Recently completed self-evaluation questionnaire revealed that the Audit Committee is fulfilling the mandate given to it by council.

2. THE INTERNAL AUDIT UNIT

The internal audit unit is fully staffed. Guided by the risk-based approach this unit has been able to address strategic issues in its quest to deliver an effective and efficient service

Allow me Madam Speaker to congratulate council on an excellent appointment to the position of Deputy Director – Internal Audit. This appointment has resulted in a great improvement in the quality of investigations as well as in the reporting format thereof.

3. INVESTIGATIONS

The internal audit unit conducted 22 investigations during the year under review.

72 findings were made of which 47 were regarded as significant (serious)

The remaining 25 findings were regarded as housekeeping i.e minor transgressions which could easily be rectified.

In most instances no findings were made i.e. that full compliance was observed.

Housekeeping transgressions appeared to indicate:

- that senior managers do not always review “inappropriate” responses by managers
- basic control deficiencies

Although widespread significant findings pointed primarily to the following areas of concern:

- lack of proper financial controls
- non-compliance
- absence of certain policies

To this end the said committees have made certain recommendations aimed at rectifying the situation. The audit committee has also requested that follow-up investigations be conducted to ensure that recommendations and improvement plans had been implemented.

Response from CFO:

We were already in the process of addressing the shortcomings and processes (part of Debtor Data Cleansing Project) when audit was conducted.

File Ref	Directorate and Function Audited	Number of Findings	Housekeeping Findings	Significant Findings
2009-009A	Financial Services – Meter Readings	2	1	1
2009-009D	Financial & Operational Services (Villiersdorp) - Revenue	5	1	4
2009-009D	Financial & Operational Services (Greyton & Genadendal) - Revenue	5	1	4
2009-009D	Financial & Operational Services (Caledon & Botrivier) - Revenue	5	1	4
2009-009D	Financial & Operational Services (Riviersonderend) - Revenue	5	1	4
2009-009D	Financial & Operational Services (Grabouw) - Revenue	6	1	5
	Totals	28	6	22

We indicated to Internal Audit that we will not develop a Risk Plan as a “desktop” exercise which is meaningless but rather a Plan which is understood and committed to by all Directorates and Risk Owners. We conducted one-on-one sessions with all management per directorate. We have achieved a lot without the Capacity.

File Ref	Directorate and Function Audited	Number of Findings	Housekeeping Findings	Significant Findings
2009-014	Financial Services - Risk Management	2	0	2
	Totals	2	0	2

We are of the opinion that the word “Investigations” should be replaced by “Audits”.

4 FINANCIAL MANAGEMENT

With the exception of a few concerns the audit committee has generally been satisfied with the standard of financial reporting and financial management within TWKM.

Financial statements are compiled by consultants. This is a costly service and maximum benefit must be derived from these consultants.

Response from CFO:

Several municipalities use consultants to save costs. Some the bigger municipalities (e.g. Eden District Municipality and Breerivier Municipality) appointed officials (CA's) who compile the municipalities Financial Statements into the GRAP Standards. The Cost of such official amounts to approximately R900 000 per annum. The cost of compiling the Financial Statements for Theewaterskloof Municipality amounts to only R180 000 for the 2009/2010 financial year because a significant amount of work is done throughout the year (eg. reconciliations, internal controls, etc.) by our own officials. Financial Statements is thus not an event and the success thereof is totally dependent on what happens throughout the year to provide accurate, complete and credible figures and source documentary proof.

The audit committee has not been able to determine the exact extent to which consultants have been able to empower internal staff. This may be an aspect deserving of future attention

Response from CFO:

TWK officials are able to compile the Financial Statements. We have been doing this for many years. It is the application and interpretation of GRAP which is a problem and you need a person who keeps track and is involved with GRAP on a full time basis as it is a moving target. If a full time person would be appointed, it would not make financial sense as indicated above (R180,000 vs R900,000 pa).

The Consultants often meet with the Auditor General and the Accounting standards Board to obtain clarity on the implementation and interpretation of the GRAP Standards. The Auditor General focuses on the Standards, if it is not interpreted correctly, it can lead to an Audit Qualification.

Positive aspects which deserve special mention include:

- an understaffed team which under difficult circumstances was able to perform reasonably well.
- The appointment of a Risk Officer
- a CFO who despite extreme challenges, has a penchant to improve financial revenue collection and financial controls. Debt collection improved dramatically during the 2009/10 financial year.
- TWKM despite inherent difficulties, is well on it's way to becoming fully GRAP compliant. With the assistance of Provincial Treasury and monitoring by the audit committee as well as clearly stated GRAP implementation plans, we believe that full GRAP compliancy will be achieved within the next two years.

Aspects which still present the audit committee with a measure of concern include:

- lack of financial controls at middle management and supervisory level

Response from CFO:

We would like to have more detail on what exactly is meant with the statement.

- Financial statements not compiled on a quarterly basis

Response from CFO:

At the end of March 2010 Quarterly Financial Statements and June 2010 Financial Statements for 2009/2010 were presented.

- monthly reconciliation of accounts and review thereof do not always occur timeously

Response from CFO:

Monthly Reconciliations are performed before the 10th Working day of the next month.

The following are amongst the accounts which are reconciled:

<i>Receipting and Banking</i>	<i>Daily</i>
<i>Creditors Statement</i>	<i>Daily</i>
<i>Bank Reconciliation</i>	<i>Monthly</i>
<i>Investments</i>	<i>Monthly</i>
<i>Loans</i>	<i>Monthly</i>
<i>Grant-in-Aid/ Trust Funds</i>	<i>Monthly</i>
<i>Payroll</i>	<i>Monthly</i>
<i>Deposits</i>	<i>Monthly</i>
<i>Assessment Rates / Valuation Roll</i>	<i>Monthly</i>
<i>Trial Balance</i>	<i>Monthly</i>
<i>Fixed Assets</i>	<i>Monthly</i>

- the 2009/10 year- end financial statement reveals a poor liquidity ratio (,7 : 1)
This suggests that TWKM is not able to meet its short term financial obligations.
It would appear that increases in employee related costs; appointment of additional personnel in key positions; consultancy fees; lower revenue collection (traffic fines) may have contributed significantly to this state of affairs.

Response from CFO:

2009/2010 Current Ratio

		Per Balance Sheet	Factual Analyses	
Current Liabilities		50,697,453	23,975,911.00	-
Consumer Deposits	6	2,942,496	-	-
Current Employee Benefits	7	11,135,961	800,000.00	
Trade and other payables	9	16,018,990	16,018,990.00	
Unspent Conditional Government Grants and Receipts	10	7,148,626	7,148,626.00	
Taxes	11	8,732,487	-	
Operating Lease Liability	18	8,295	8,295.00	
Current Portion of Long-term Liabilities	3	4,710,598	-	
Current Assets		36,348,694.00	43,202,593.00	
Inventory	16	97479	97,479.00	
Trade Receivables from exchange transactions	17	17255360	17,255,360.00	
Other Receivables from non-exchange transactions	17	6554895	6,554,895.00	
Unpaid Conditional Government Grants and Receipts	10	29538	29,538.00	
Operating Lease Asset	18	1603760	1,603,760.00	
Taxes	11	3439592	3,439,592.00	
Current Portion of Long-term Receivables	15	6320	6,320.00	
Cash and Cash Equivalents	19	7361750	7,361,750.00	
Advances from TWK Funds to Finance Loans			6,853,899.00	
		14,348,759.00	-19,226,682.00	
Ratio		0.72	1.80	

- Own funds - Temporary Advance to Loans (approved & guaranteed) equals R 6,853,955.
If only this is incorporated into the Balance Sheet, the ratio will change from 0.72:1 to 0.85:1.
- Consumer Deposits (6) - It is not payable in the short term. It can also be offset from Debtors because it is meant to redeem irrecoverable debts.
- Short term Portion of Long-term Liabilities (3) (R 4,710,958) - It is also payable in 2010/2011 from 2010/2011 Revenue. It is budgeted for in 2010/2011 Revenue.
- A significant increase in Current Employee Benefits (11) has also contributed to the decline in the Liquidity Ratio (from R 6,588,583 to R 11,135,961). The likelihood that this full amount would be paid out is almost zero. The main reason for the escalation is because long-service bonus was not applicable to all employees.

The table below provides an indication of the short-term portion of the liability. The R800 000 is a more realistic figure. The balance of R6 348 626 should therefore appear under long term liabilities.

	2008/2009	2009/2010
Long Service	108,885.00	293,712.00
Leave	674,787.00	454,447.00
Total	783,672.00	748,159.00

- Trade Receivables (17) has been significantly understated at R17m (too conservative). The methodology is too much of an Accounting Calculation instead of facts of recovery of the debts. This figure should at least be R50m based on facts and the collection trends in different towns, improving collection rate in farms, etc. Golf Estate: out of court settlement has been reached and this will ensure a reliable payment rate with effect from 2010/201. During 2009/2010 Financial year we have introduced the blocking of Electricity when accounts are in arrears and Prepaid Water Meters are being rolled out. In 2010/11, Electricity Prepaid Meters are introduced to all households. This will significantly improve collections.

TWK Municipality has 59 Debtor Categories (most municipalities have between 4-8 categories) which has assisted a great deal in dealing with debtor, different approaches, improved assessment of recoverability of debts, etc. The fact that the Debtpack System is almost fully functional is contributing a great deal to the recovery of outstanding debts.

It should also be noted that Cash Receipts from Ratepayers, Government and other (Non- Exchange Transactions) increased from R99m to R136m (R37m or 37%)

- *Taxes (11). This amount should not reflect VAT on outstanding debtors; it is not a liability because we are registered on the Cash Basis and not on the Income Basis. Secondly this amount represents 50% of the Total amount reflected under Trade Receivables in Note 17 (R17, 255, 360).*

Conclusion

- *With all these changes incorporated into the Balance Sheet, the liquidity ratio will change to a ratio of 1.8:1.*
 - *The use of ratios in GRAP for the public sector does not project the correct status of financial position.*
- a net cash outflow of almost R30m over the past financial year.

Response from CFO:

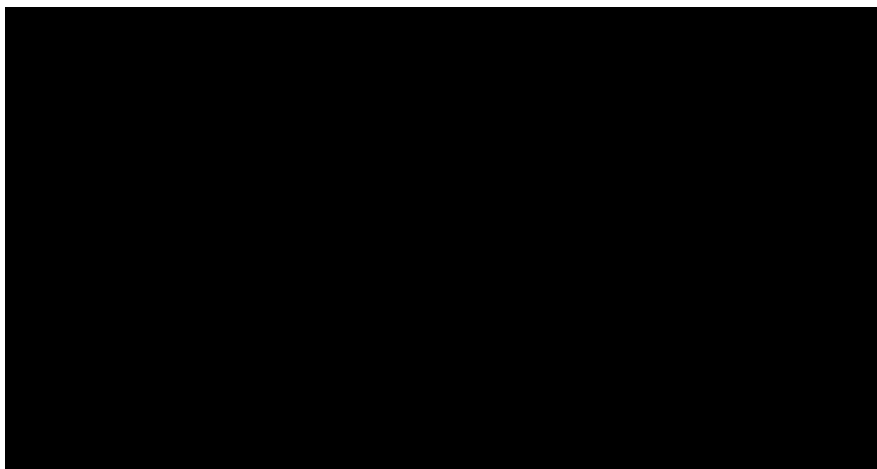
This is caused primarily by the following:

- *In 2008/2009 an amount of R33,391m New Loans were raised compared to R15,287m which would only be paid in 2010/2011 financial year (Cash from Financing Activities)*
- *Cash Payments to Suppliers and Employees increased from R157m to R197m, ie R40m (25%)*
- *On the Positive side Cash Receipts from Ratepayers. Government and other Non-Exchange Transactions increased from R99m to R163m (R37m or 37%)*

- over-expenditure in a few capital item votes

Response from CFO:

According to Annexure E(2), no overspending according to Votes on Capital. In terms of the MFMA a "Vote" may not be overspend. This means that you may have some line-items overspending as long as the vote is not overspent. We however attempt by all means not to overspend line-items.



There is no over-spending by Vote as per table below

- a few minor corrections to income statement are required.

5. PERFORMANCE MANAGEMENT

Performance Management is increasingly featuring on the radar-screen of the Auditor General. It is for this reason that a Performance Audit Committee was established during the previous financial year.

The purpose of Performance Management is to ensure that Performance is measured against pre-determined objectives and that reporting thereof is reliable, accurate and complete.

It pleases me to inform that considerable time and effort has been invested in Performance Management by the responsible directorate. A very comprehensive process plan, which in essence is the IDP process plan has been approved by council.

Due processes were followed and quarterly performance reports were found to be complete and in most instances submitted timeously to the performance audit committee..

A few teething problems are however still evident

- There are still too many KPI's and they should be reduced in order to make them more manageable.
- A few of the objectives appear to have been too ambitious
- A few of the objectives and KPI's were found not to be measureable.
The age-old adage **"If you can't measure them you can't manage them"** is a self-evident truth.
- The allocation of performance bonuses to executive directors still pose a challenge even though due processes were followed

6 SERVICE DELIVERY

Given the many challenges which face municipalities in their quest to provide a quality service there appears to be sufficient evidence which supports the view that TWKM is doing remarkably well in this area. Investigations by the internal audit unit, and more importantly, reports submitted by executive directors have provided the audit committees with assurances that service delivery to say the least is satisfactory.

In this regard it needs to be mentioned that TWKM was selected as the top service delivery local authority in South Africa at the African Access National Business Awards ceremony in Sandton on 27 May 2010

7. LEADERSHIP

Both the Executive Mayor and Municipal Manager need to be singled out for the quality of leadership they bring to TWKM.

There is ample evidence which points to the fact that the Mayor and Municipal Manager are strategic in their thinking. Through the risk-based approach they have been able not only to identify key control areas but to implement strategies and to monitor and regularly report on them.

8. APPRECIATION

Allow me Madam Speaker to express my gratitude to:

- Council for providing the necessary leadership
- The Executive Mayor for his insight, support and passion to serve.
- The Municipal Manager and his Executive Directors for their participation in audit committee meetings and for the very positive manner in which they have responded to recommendations by the audit committees.
- Employees of TWKM.
- The Deputy Director - Internal Audit and his team for the quality of their investigations as well as the quality of their reporting.
- Members of the audit committees for discharging their duties in such a competent manner.

I thank you.

C. Martin
(Chairman - TWKM Audit and Performance Audit Committees)
28th October 2010